

## Work and Pensions Committee

### Oral evidence: Pension Protection Fund and the Pensions Regulator, HC 55

Wednesday 23 November 2016

Ordered by the House of Commons to be published on 23 November 2016

[Watch the meeting](#)

Members present: Frank Field (Chair); Heidi Allen; Ms Mhairi Black; Ms Karen Buck; James Cartlidge, Neil Coyle; John Glen; Richard Graham; Luke Hall, Craig Mackinlay; Steve McCabe.

Questions 3425 - 3501

#### Witnesses

Lesley Titcomb, Chief Executive, the Pensions Regulator, and Andrew Warwick-Thompson, Executive Director of Policy, the Pensions Regulator.

Richard Harrington MP, Parliamentary Under-Secretary of State for Pensions.



## Examination of witnesses

Witnesses: Lesley Titcomb and Andrew Warwick-Thompson

Q3425 **Chair:** Welcome. Might you identify yourselves for the sake of the record, and then we will begin?

**Lesley Titcomb:** I am Lesley Titcomb. I am the chief executive of the Pensions Regulator. Good morning.

**Andrew Warwick-Thompson:** Good morning. I am Andrew Warwick-Thompson. I am the executive director for regulatory policy at the Pensions Regulator.

Q3426 **Chair:** Lesley, I wonder whether you might bring us up to date on BHS and Arcadia, so that the general public understand the use of your powers. To what extent are you now pursuing Sir Philip's assets to try to get a just settlement for pensioners? What has he offered you and would your powers, for example—as many of the papers are interested in—extend to assets such as his boats?

**Lesley Titcomb:** Chairman, first of all, I would like to assure the BHS pension scheme members that we are relentlessly pursuing the best possible outcome that we can secure for them. To that end, as you know, on 2 November we issued a warning notice giving an indication of our intention to attempt to use our powers against various targets. That followed a period when we had been pursuing twin tracks, as you know: our investigation, which then led to the issue of that warning notice; but in the meantime, over the summer, a period of negotiation about a possible settlement. The point was that we had reached the conclusion of our investigation and, by that point, we had not received a comprehensive and credible offer, so we went ahead and issued the warning notice.

Q3427 **Chair:** Can I interrupt? It is almost six months since Sir Philip said before this Committee that he would sort it. The six months is almost up, isn't it? You have been quite a long time trying to get a settlement out of him, haven't you?

**Lesley Titcomb:** In these circumstances, it is important to understand that our door is open to the parties to approach us at any point, but in the meantime we pursue the investigation as rigorously as we can. As we had not received a comprehensible and credible offer, we went ahead and issued the warning notice. What now happens is that that is a statement of our case to the parties. They have a chance to absorb that and to make any representations they wish to make. We then review those and determine whether we are going to then take the case to our determinations panel. That is a committee of people who are not connected with the staff of the organisation, and the power to exercise



## HOUSE OF COMMONS

the enforcement powers to make a contribution notice or a financial support direction is reserved to them by law.

They will set their own timetable as to when that hearing happens. I would have thought that that is unlikely to be before the middle of next year. In the meantime, our door remains open to any further offers. If the determinations panel goes ahead and confirms the exercise of our powers, then it is open to the parties concerned to refer that decision to the upper tribunal—a form of appeal—and again the timetable is completely out of our hands. The upper tribunal is part of the courts' mechanisms.

Assuming that either at the determinations panel stage or the upper tribunal stage, a contribution notice is confirmed and issued, or a financial support direction, then a contribution notice effectively creates a legally enforceable debt in favour of either the scheme trustees or the PPF, depending on the circumstances. The scheme trustees or the PPF can then enforce that debt through the courts in the normal way.

In terms of a financial support direction, that is a decision, in principle, that a person or company owes support to the scheme. A period of discussion and negotiation then ensues as to the form of that support, and there is great flexibility as to what can be taken into account in those situations.

I hope that explains the next stages of the process.

**Q3428 Chair:** Lesley, given that we have seen moneys going to Lady Green—although the main player in all of this has been Sir Philip—where would you be looking for the assets that might satisfy a fairer deal for the pensioners?

**Lesley Titcomb:** In both cases, as I have said, there is a degree of flexibility here because the contribution notice creates a normal debt that would be enforceable in the normal way, and I imagine that, should push come to shove—and it must really get to the end of this process, but we are very much at the earlier stage at the moment—the court would take whatever normal steps it would to enforce that debt.

If we are talking about either a settlement or a financial support direction, then essentially what we are looking for there are sources of support for the scheme, which could be cash or guarantees or some other structure and, as I have said, there is a great deal of flexibility as to what could be taken into account. Having said that, whatever is proposed under either of those routes we need to be absolutely sure it is robust and does not in a way create a continuing risk for either the members or the PPF. For example, we would want to ensure that any assets that were being offered would be properly valued. We would not just take an offer like that, so I hope that explains how we would go about this.

**Q3429 Chair:** But would it be the courts that would look at the assets that they



## HOUSE OF COMMONS

would seize to try to meet what you require as a sum that is due to the pension scheme?

**Lesley Titcomb:** Yes, that's right, if we are talking about a contribution notice that creates a normal legally enforceable debt to the scheme. It would then be the scheme trustees or the PPF who—with our full support, in any way, shape or form that we could offer, I might add—would seek to recover that debt through the courts, and the court would determine how that was to be achieved.

Q3430 **Chair:** The courts would determine whether the assets were owned by Lady Green or Sir Philip Green?

**Lesley Titcomb:** I believe that is right. As you know, our warning notices are specifically targeted on certain targets, so the debt would be created against those targets, and I imagine the court would have to go through its normal process of assessing that target's assets.

Q3431 **Chair:** Has your notice frozen assets that might be considered to be used for the debt?

**Lesley Titcomb:** No, we do not have the power to do that.

Q3432 **Chair:** Would you like that power?

**Lesley Titcomb:** As I have said, I think things are at a very, very early stage at the moment; we have only issued a warning notice. It is our determinations panel that will determine whether or not that power is definitely being exercised, and there are considerable elements of the process that may still then be gone through, so I think it is far too early to speculate on how that might pan out. I don't see access to assets as an immediate problem in pursuing anti-avoidance investigations at the moment.

Q3433 **Chair:** On the proposals that Sir Philip has put to you, is it that the sum isn't large enough or that delivering the sum has been the problem?

**Lesley Titcomb:** The Committee will understand that I am reluctant to discuss the precise terms of settlement offers and so on. However, what I can say is that, if it was as simple as a cheque being written then I am sure we would all be happy that—if it was for the right sum—that would be a very good outcome for the members.

Q3434 **Chair:** It could be the outcome, though, couldn't it?

**Lesley Titcomb:** It is one of the options that is still there; you are absolutely right. However, if the offer takes a more complex form in some way, then we have to not just be satisfied that the monetary amounts are correct, but also ensure a good outcome for the members; that there isn't any residual risk falling on either the members or, indeed, the PPF, because we also have to protect the PPF. That is why it isn't just about money. For example, it may also be about the structure of any deal that is offered.



## HOUSE OF COMMONS

Q3435 **Chair:** It is not the first year; it is maybe the 30th year and the delivery of the funds?

**Lesley Titcomb:** Absolutely. If there is some ongoing element and ongoing commitment, we absolutely have to ensure that that is robust.

Q3436 **Chair:** My last question—partly because the public have been lobbying me over it, because they are so obsessed, and rightly so—is about his ostentatious display of wealth with his boats. That might be for the courts to decide whether they have to be sold, rather than you. Is that right?

**Lesley Titcomb:** That is correct.

Q3437 **Richard Graham:** In terms of where the pensioners are at the moment, the pension scheme is still managed by the trustees, and still chaired by the previous chair, Chris Martin. At what stage during the legal process was there any discussion about whether the pension fund should move into the stewardship of the PPF?

**Lesley Titcomb:** The scheme at present is in what is called the PPF assessment period, which is a period when there is a strong possibility that it would go to the PPF. In the meantime, the PPF is administering the payment of the pensions of those who are receiving pensions from the scheme. Of course, what we don't yet know, given the shape of any settlement, is whether it would be possible for a scheme to come out of the PPF and continue in some form, or whether the PPF would receive sufficient funds that it would be able to buy out the benefits of the members at better than PPF levels.

Q3438 **Richard Graham:** To be absolutely clear on this, what are the responsibilities of the trustees at the moment and who is responsible for making sure that, as far as possible, the assets are still delivering what is required in terms of the pension streams?

**Lesley Titcomb:** As I understand it, the PPF is very closely involved in the administration of the scheme. The trustees are still in place but the PPF is working closely alongside them. I believe that is correct.

**Andrew Warwick-Thompson:** That is correct, yes.

Q3439 **Chair:** Are there some pensioners who are in a sense suffering PPF cuts to their entitlement, even though the scheme in total is not within the PPF?

**Lesley Titcomb:** My understanding is that the vast majority of pensioners who were in payment at the time of the administration are continuing to receive their full pension.

**Chair:** In full?

**Lesley Titcomb:** That is correct, yes.

**Richard Graham:** So no haircut?

Q3440 **Chair:** But what about the new ones?



**Lesley Titcomb:** The new ones who enter will be haircut for the moment, but if the settlement results in better than PPF benefits for members, then whatever amount of that haircut is appropriate would be refunded to them.

Q3441 **Chair:** What is the date at which pensioners reaching their retirement age, as Richard said, were being haircuted? When did that process start?

**Lesley Titcomb:** I believe it is the date of the administration, but I am not an expert on the PPF operations.

Q3442 **Chair:** It has already started in effect, hasn't it?

**Lesley Titcomb:** I believe so.

**Richard Graham:** What we could do, Chairman, is ask the PPF to give us a written clarification of that, and confirm that all the new pensioners affected are being written to in advance with a clear explanation of what is happening and what the process is.

**Chair:** How they see that process working, building up in the weeks and months ahead?

**Richard Graham:** Yes.

**Lesley Titcomb:** The PPF is very experienced in managing these situations and I am sure would be able to explain that to you.

**Chair:** Brilliant.

Q3443 **Richard Graham:** Moving on to the wider issues, Lesley, as you know, the evidence we took focused on three areas. First, does the Pensions Regulator need new powers? Secondly, could it exercise its existing powers more robustly? Thirdly, do you need more teeth for your existing powers? You have submitted a pretty detailed written outline of your roles and powers. I don't think there is any point in asking you to recap all of that, because it is on the record.

**Chair:** I agree.

**Richard Graham:** Lesley, can you give us a bit more detail on what some of your responses to those three areas might involve? For example, you have talked about a further evolution of your operational approach to focus more intensely on schemes that present the greatest risk. How would you decide what those schemes are? Would it be through an analysis of the pension fund's assets and liabilities, or would it be on an analysis of the corporate sponsor situation, or a blend of both?

**Lesley Titcomb:** First of all, I would like to say that I have 500 staff, based in Brighton, who are absolutely committed to working for the benefit of the members of the occupational scheme, so we regulate as hard as we can within the framework that Parliament has set for us. Witnesses here, and our submission to you in some cases, have suggested that we may require certain new powers and we have set those out for you. It is also about how we operate internally, and I would



## HOUSE OF COMMONS

like to say a little bit about that. That also has some implications around resources.

We have been operating the regulatory regime for 10 years now, since the TPR was set up. That has given us an insight, both into aspects of the legislative framework and our powers, but also I think it is time to do a drains-up on how the organisation operates and makes the choices that are within its own discretion to make: how we use our resources and how we select which cases to follow up, as you indicated, Mr Graham.

In particular, we want to be quicker and more responsive. We want to be taking quicker decisions about where our powers may be used. We have very much emphasised what we call education enablement, trying to bring the trustees and employers to agreement, and I think we can move quicker to concluding that that is proving challenging and that we need to consider the use of our powers. I think we can be clearer in our expectations of trustees and employers, both in terms of the guidance we offer and in terms of when we engage with individual schemes; being clearer about what we expect them to do, and by when we expect them to do it.

When I arrived at the organisation as a new chief exec, as you would expect, I went around and spoke to stakeholders. I heard some of the things that you have heard from witnesses in front of this Committee: that sometimes people perceive us as being reluctant to use our powers. That is something I have been focusing on with the organisation since I arrived. We are making considerable efforts to use a wider range of our powers more innovatively. For example, we have just started our first criminal prosecution for non-compliance with a section 72 information order.

**Chair:** Luke is going to come on to that.

**Lesley Titcomb:** Yes, absolutely. This of course can have an impact on resources, but it would be irresponsible of me to sit here and say it is all about more resources. It isn't. It is about how we use our resources more effectively, which is why I have kicked off this piece of work, which we expect to run over the next four to six months, that will look at our whole approach to regulation—not just DB but DC public sector as well—as to how we can do this better in the way that I have described. We may need more resources coming out of that.

We may need more resources if we decide that it would be sensible to change our risk bars, which is the question: how do we choose what we follow up on? We have a series of triggers in any particular situation, but to answer your direct point, when we are looking at the funding situation of a scheme and which ones present the greatest risk, we obviously look at what we call the scheme-specific valuation of assets and liabilities, but we also look at the strength of the employer, which we refer to as the covenant. It is those factors that we take into account, but it is very scheme-specific.



Q3444 **Richard Graham:** In general terms, it looks to me as if your challenge in a sense is not dissimilar to that of Ofsted or the Care Quality Commission. You have to identify who is basically fine and doesn't need any attention, which are the ones that are critical and need a lot of attention right now, and which are the ones coming up that are likely to pose a problem. That involves making some quite difficult but very important decisions on who are the likely patients coming your way. That is a skillset that has been a bit glossed over in the past.

**Lesley Titcomb:** You are absolutely right to identify it as a key area of focus for any regulator as to how you best use your resources and having a systematic way for making those choices. There have been a number of comments about the skills and capability of TPR, if I may just address that.

We do absolutely constantly face the challenge of trying to recruit good people, as does any organisation in our position at the moment, but what I will say is that we have staff of many different capabilities, including lawyers from magic circle firms. Our business analysts, who are absolutely key in doing the kind of analysis you describe, Mr Graham, tend to be from the big chartered accountancy firms or from restructuring operations in banks, so they understand group restructuring and that type of thing. So we are able and we do have very good people, and we will continue to do that and we will continue to be out there trying to add to that cadre of people.

We are trying to drive up our regulatory capability as well, so I have reorganised the regulatory front-line function and we are recruiting more staff at a senior level there to bolster that.

Q3445 **Richard Graham:** In terms of the objectives that your restructuring is going to effectively address, obviously there is this difficult balance between protecting members of schemes, the risks for the PPF, and also minimising any adverse effect on companies' ability to grow. When you laid out the Pensions Regulator's objectives, we also noted Chris Martin's comment that clarifying statutory objectives and potentially conflicting objectives would be useful. Do you see that there is any contradiction between minimising companies' ability to grow while protecting members' interests, or do you think that the objectives as they are can be achieved?

**Lesley Titcomb:** I do believe the objectives can be achieved. They can sometimes be in tension, which is inevitable. What I would say is that I think we all accept that the best security for a defined-benefit scheme is a thriving employer. That is absolutely why having regard to the sustainable growth of the employer is, and always has been, an important part of what we do.

There is one important point—Andrew might wish to add to this—which is that we do believe that there is an opportunity here to be clearer with





## HOUSE OF COMMONS

schemes and with employers about what “good” looks like in terms of funding arrangements and recovery plans.

**Andrew Warwick-Thompson:** Yes. The regulator came into being as a result of the 2004 Act, and we were moving away from MFR, the minimum funding requirements; everybody migrated themselves down to the lowest possible level. It was deemed to be unsatisfactory, so we now have this more flexible approach.

As a regulator, we have tended to steer clear of saying what is good or what is bad. We have given a lot of guidance to trustees and, indirectly, to their advisers. We are now looking more closely at being clear about what we expect, particularly in relation to two terms that are used in the legislation, which are not well understood: what is prudent; and what is appropriate? Talking to stakeholders, as we have done on a continual basis, we think that some further guidance and clarity about what we mean by that or how we interpret the legislation would help trustees and their sponsors come to better arrangements in relation to the funding of their schemes.

Q3446 **Richard Graham:** Yes. With the business of prudence and holding Government bonds and stuff, the definition of that might vary over time.

Can I finish by asking one little technical question, Chairman? Lesley, in terms of what might happen when a scheme is in this situation of purgatory, which you were just describing for the BHS scheme, where the trustees are still there but the PPF is administering it and new pensioners are taking a haircut on the amount of pension they are getting, if in due course, in a situation like that, you do reach a settlement with the sponsor and an amount of money is agreed in a format that is acceptable to keep the pension scheme out of the PPF, is there any recourse effectively for pensioners who have taken a haircut for a period of time—perhaps a year—to be reimbursed the difference between what they received and what they should have received under the pension scheme obligation?

**Lesley Titcomb:** We would have to look at that, as part of any potential settlement, and see how that might work within the arrangements of any particular proposal that is on the table. In the simpler situation where perhaps a sum of money is provided, which enables the PPF to then buy out better benefits than it can offer for the members, then I believe there is provision for that kind of haircut to be addressed, yes.

Q3447 **Richard Graham:** It would certainly seem that that should be in the spirit of the phrase of any commitment to sort a pension fund.

**Chair:** It would have two tiers of pensioners otherwise, wouldn't it?

**Lesley Titcomb:** Potentially, yes. That is why we would need to look at it, if it was the type of situation you describe, Mr Graham, and, if not, then the PPF thinks about that in those particular situations. They would be better placed to answer you.



Q3448 **Luke Hall:** Lesley, can I ask what you are doing to ensure that sponsors are co-operating and sharing information with trustees and the TPR, and what information is needed to be shared?

**Lesley Titcomb:** First of all, can I acknowledge that in the vast majority of circumstances we have a very, very positive relationship with trustees and employers, and most sponsoring employers behave entirely responsibly and it is important to note that, and they co-operate with us.

What we seek to do here obviously is, first of all, to support trustees through educating and enabling them, so that they can have good and constructive relationships with their sponsors. That happens in the vast majority of cases, but sometimes we have to recognise that, for whatever reason, they are not making progress. Perhaps the information isn't flowing and that we need to intervene in some way, so we may ask for information to be provided for us so that we can better understand the situation.

At the moment, the only power we have to ask for that information is the section 72 power with a criminal sanction attached. In other areas of our regulatory forest, we have been given an information gathering power, which is much more typical of other regulators. That is a power like that but with a civil sanction attached, less heavy handed and with a lower bar to achieve in terms of proving non-compliance. We are very keen to have in our DB and normal DC regulation a power similar to that, which we have been given in auto-enrolment and master trust regulator, and I will hopefully be given that if Parliament agrees on master trusts.

**Chair:** The Bill has started in the other place.

**Lesley Titcomb:** Indeed, and I am very pleased about that. However, we also think that this may also be addressed by having a general duty to co-operate on employers and trustees. Again, this is typical with other regulators as well. We are exploring the possibility of these with the Department for Work and Pensions.

The final point I would say here is that, when we do get into investigation situations—as we do occasionally—we don't at present have a power to compel people to attend an interview, so we are reliant on this quite blunt tool of section 72, which can result in receiving a lot of information and we cannot then necessarily follow up and narrow that down. We can ask nicely for somebody to come and talk to us, but we cannot insist. We are exploring the possibility of that power as well.

Q3449 **Luke Hall:** Thank you. You mentioned in answer to Richard's question earlier about the use of your section 72 powers. I wonder if this is an example of where you would be more proactive, I suppose, to avoid the collapse of schemes, and whether this is an indication of section 72 being used again in the future.

**Lesley Titcomb:** We use section 72 fairly liberally—several hundred over the past couple of years. It is a very heavy handed approach, when you



## HOUSE OF COMMONS

are engaged in a non-confrontational regulatory relationship with someone, to be approaching them with an information gathering power with a criminal sanction attached. Also, as we look at our regulatory approach through the project that I described, which we are just undertaking, we will want to, with certain segments of the population—for example, stressed schemes—get into having a more ongoing relationship and exchange of information with them. We will want to ask for information in those circumstances, knowing that we have the power of the law behind us but we will want to encourage a more co-operative and typical regulatory relationship.

Q3450 **Chair:** Might you explain a little bit about why you had to press the nuclear button in dealing with Arcadia? Is that partly the lessons you have learnt from BHS?

**Lesley Titcomb:** If I may, Chairman, we set out very clearly in our letter to you what the situation was in terms of our engagement with Arcadia. I do not have much further to add on that, except to say it is one of a number of schemes that we engaging with, in the normal course of our business, and we keep it under watch, as I said to you in the letter. It is not untypical for us to use section 72 notices in such situations to get information in relation to a particular question.

Q3451 **Chair:** Parliament has the right to send for papers and people. We found it quite difficult to get information out of Arcadia, so we sympathise with the problems you are having. Do you think the Arcadia trustees would be strengthened if they had at least one or more independent members, rather than all practically staff appointments?

**Lesley Titcomb:** I would not want to comment on any particular situation, but ensuring trustee capability and the right skills on a trustee board is absolutely essential. We have been doing a lot of research on what makes effective 21st century trustees, and we will be publishing more about that over the coming weeks. There is no doubt that independent trustees can bring something to the party. There are some good ones out there but they are quite few and far between. It is something we want to look at. For example, if we are faced with schemes that are underfunded and have a stressed employer, should we look in such situations at appointing a new trustee?

Q3452 **Chair:** You do not have powers at the moment to do that, Lesley?

**Lesley Titcomb:** We absolutely do.

**Chair:** You do have them?

**Lesley Titcomb:** Yes, and we do exercise those powers.

Q3453 **Chair:** Is there a good pool of people you can draw upon?

**Lesley Titcomb:** There is a pool of good people, but not a particularly large pool.



Q3454 **Richard Graham:** Just very briefly on the trustee point, it has been mooted that maybe all schemes should have an independent trustee. Do you think that is a bit of a blunt instrument and that it should be about selecting which schemes need one, or do you think there is a case for it in principle?

**Lesley Titcomb:** Certainly, from a regulatory perspective, and the types of situation that the Chairman was referring to, you would use it as a selective tool. There is a wider challenge about driving up standards of trusteeship, as we have mentioned. The role of independent trustees in that is also worth considering but, as I said, the pool is small. There is a cost involved with that. There are other aspects that could be looked at and we may come on to. For example, is consolidation of some schemes appropriate and would that have the same effect?

Q3455 **Chair:** Are you going to bless Arcadia's pension scheme with an independent trustee?

**Lesley Titcomb:** At the moment I have nothing further to add to what I said in my letter to you on Arcadia. We are keeping the situation under review.

Q3456 **James Cartlidge:** I want to ask about recovery plans. What length of recovery plan is acceptable to you, and can you expand on what are the most important factors in determining that?

**Lesley Titcomb:** Sure, absolutely. First of all, if I may give you a couple of statistics: 99% of recovery plans are less than 25 years in length, and those that are over are a very small number in very, very specific circumstances. Some 80% of recovery plans are under 12 years, and what we see from the most recent sets of valuations we have been looking for is that the average length is about eight years. It is important to understand that, when we are looking at the funding position of a scheme and any associated recovery plan, we are doing that in a very scheme-specific way. That is what the system is set up for us to do, so we don't just look at length; we also look at the structure. For example, we have a series of triggers when a recovery plan is presented to us and we look at whether any of those triggers of concern are there. A good example would be back-end loading of the payments, particularly if the employer was suffering from decline in profitability; that type of thing.

Q3457 **James Cartlidge:** In terms of the size of the companies, because obviously it is a very interesting statistic, the concern would be that there would be very large schemes and are they more likely to have longer? Obviously, if they have a larger deficit they will need longer and so on. What is causing the length fundamentally?

**Lesley Titcomb:** It will be principally about affordability for the employer. That is the principal driver. If we have a concern around a recovery plan, the discussion would then usually hinge around what the employer can afford to pay.



**Andrew Warwick-Thompson:** I can give you some more statistics on that if you would like me to. If we look at this from the narrow position of affordability, there are about 1,000 schemes that we believe have broad affordability issues, so those are the ones we tend to look at most closely. Then the total size of the scheme-specific deficit: for those schemes it is about £40 billion and that is skewed towards the larger end, so very large schemes; those are the ones that have more than £1 billion-worth of assets and account for maybe £17 billion-worth of those deficits. In terms of the length of the recovery period, there are about 150 schemes that have recovery plans and, within this affordability group that we are looking at, about 150 schemes that have recovery plans that are greater than 18 years at the moment.

Q3458 **James Cartlidge:** What is the longest?

**Andrew Warwick-Thompson:** It would be in excess of 26 years, probably, but there are very, very few.

**Lesley Titcomb:** Your point about whether it tends to be the larger schemes that have the longer recovery plans is true. It is not absolutely true the whole time, but it is true that there tends to be a bias towards the larger schemes and the longer recovery plans.

**Andrew Warwick-Thompson:** But nearly half of those schemes will have a recovery period; so 561 schemes have recovery plans; even in this affordability-issue group they have recovery plans of less than six years.

**Lesley Titcomb:** Yes. What we would typically do in this situations is, first of all, encourage the trustees to challenge the employer as to whether they really have ensured that they are paying everything they can afford to pay in. But as we have said before, it is a thriving employer and one certainly that continues in business that is the best security for the scheme, so we don't want to unnecessarily drive the businesses out of business here.

Q3459 **James Cartlidge:** But does it vary? Is it a moving feast? If the company's performance improves, can they come back to you and reduce the—

**Lesley Titcomb:** Absolutely. How this generally works is around the three-year valuation cycle. They have to submit the three-year valuation to us and, if they are in deficit, a recovery plan associated with that, so it is essentially driven around the three years. We collect a certain amount of information in the meantime, and the trustees, who are the first line of defence here, will be monitoring the situation in the meantime.

If the employer wishes to vary the recovery plan in some way, they can come to the trustee and ask to do that. We have seen the odd example of that where, for example, the employer has come and made a case to the trustees that there is an opportunity to invest in a new development in the business and that, say, a two-year suspension of the recovery plan



## HOUSE OF COMMONS

would help them to do that, and then increase the strength of the employer going forward. The trustees agreed to that. We were okay with that, and that then went on and they were able to invest in that business at that point, and then the position of the scheme was actually strengthened because the employer was thriving.

**Q3460 Chair:** Lesley, in the sense that a theme of about eight years is emerging, is that figure coming down from Mount Sinai, or is it being prodded by you, or is it schemes that have independent trustees that are pushing for recovery plans of about that length of time?

**Lesley Titcomb:** As we said, Chairman, we try to be clear with the population and we think we can do more on this, as to what good funding structures and good recovery plans look like. The figure I gave you of eight years is a statistical fact of the existing ones. As I said, what happens is that when we receive the valuation and the recovery plan we look at it to see if it hits certain triggers and, if it does, we will follow up and discuss with the trustees to see whether there is something that needs to be amended in that; to see whether they are challenging on the right things.

As we have also said to you before, there are a number of schemes where we actually engage with the trustees and the sponsor during the valuation process, so that we can make sure that some of our concerns are being addressed upfront. We call those proactive cases. We are seeking to do more of those because we think we get better regulatory leverage through doing that.

**Q3461 Chair:** In terms of a good trustee and an independent trustee, with this figure of eight years you are beginning to set a culture, aren't you, about when you expect recovery processes to be complete, unless one can make special exemptions to it?

**Lesley Titcomb:** That is why we are looking, for example, at whether we should publish further general guidance on funding outcomes and recovery plans, so that scheme trustees of any type can see where they fit into the overall spectrum and they can see whether what their employer is presenting them with is unusual. But we do, as you can imagine, cover a number of these aspects in, for example, our training for trustees and, as you have identified, professional trustees in particular will have expertise in this area.

**Q3462 Chair:** To have had that information would have helped BHS's trustees, who settled for 23 years, wouldn't it?

**Lesley Titcomb:** As you know, Chairman, in those situations we do follow up and we ask the question. We would be signalling very clearly to the trustees that we thought such an arrangement was unacceptable, not just because of the length but because of other aspects as well.

**Q3463 Luke Hall:** On consolidation, what are the main barriers now to consolidating schemes and what are you doing to overcome this?



**Lesley Titcomb:** We think consolidation could be valuable, both in the DB and the DC market, because it could bring benefits of scale, cost savings, and drive up standards of trusteeship. I will ask Andrew to say a bit more about the challenges here, because on the DB side in particular it is not easy to achieve. We are seeing aspects of it—Andrew can talk about that—but it is challenging here.

**Andrew Warwick-Thompson:** Yes, there are a number of large companies that, for historic reasons, have ended up with a lot of pension schemes. Several of those have attempted to consolidate the administration and the governance of those schemes. A simple model of that would be that the trustees of all these schemes remain in place but they share administration platforms and drive the cost of administration down. They may share common advisers and they may share a secretariat function.

Some companies have gone further than that and have created asset pools. They have done that for very similar reasons to the LGPS: you get more bang for your buck if you put the money together, and you can drive down the costs. A few of them have gone further still and have created a unified board of trustees, so that unified board is then responsible for all those schemes within that group of companies. That is a relatively small group of companies. They tend to be very big—they are typically within the FTSE 100—and have a lot of resource.

When you move outside of that and you get into the realm of non-associated employers, it becomes much more difficult. Trustees and the sponsors are reluctant to cede control under those circumstances, and I would suggest that, because no commercial model of that has evolved over the last few years, it is probably because it needs a bit of a push. That may need some regulatory or legislative intervention.

Where we have considerable problems, though, is going beyond just the consolidation of services and assets. Where you try to consolidate the liabilities, that implies that you are somehow severing the link with the sponsoring employer who provides the covenant, and that is really the biggest difficulty with DB schemes. We see huge potential, particularly for those small subscale schemes for bringing them together to support better funding outcomes by reducing their administrative investment and governance costs through some form of consolidation.

**Lesley Titcomb:** The challenge will be: will that happen naturally through the market or is some legislative intervention needed, for example, to make it useful in particular circumstances, if we felt it was an appropriate technique for dealing with subscale schemes that had a stressed employer or something like that. Those are issues we are discussing with the DWP.

Q3464 **Richard Graham:** Lesley, I think that is a really interesting point, because all of these trusts are set up separately and they all have slightly different legal structures and so on. Therefore, the biggest obstacle to the



## HOUSE OF COMMONS

consolidation that Luke was talking about is how you bang them all together. Even if the trustees are willing, the amount of governance to go through in terms of approval of members and all the rest of it is quite hefty. If there was a relatively simple way through legislation of enabling that, it seems to me much more likely to get this ball moving fast. Would you agree with that?

**Lesley Titcomb:** If it is to be made to move faster, then some sort of legislative intervention is likely to be required, if we think it is the right thing to do in order to improve funding through cost saving, through better investment and through better trusteeship. But it has to be properly explored to check we don't have any unforeseen consequences and, as Andrew said, for example, anything that starts to divorce the connection with the employer can be problematic and you are losing the most important source of support then.

**Chair:** Luke, are you happy with that? Can we go on?

**Luke Hall:** Yes.

**Chair:** All right, Stephen.

Q3465 **Steve McCabe:** I want to ask about clearance. It seems that fewer employers are using clearance now. I wonder why that is.

**Lesley Titcomb:** You are absolutely right. When clearance was first introduced in the early days of TPR, we were getting between 200 and 300 applications a year. This year we have 15 on stops, so there is a difference and we believe that this is due to the fact that clearance was established solely as a mechanism for the buyers and sellers in corporate transactions to get comfort that we were not going to come after them with our anti-avoidance powers.

We believe that over time those buyers and sellers who tend to be well advised have understood the parameters of what needs to be done to ensure the safety of a scheme in such corporate transactions and, as I have emphasised, the majority of people do behave responsibly. Therefore, they don't need to go through the process of clearance.

That is fine, but there are some questions that follow from that. For example, is there enough of an incentive on people to really think that through? Could there be more of an incentive for those who are not behaving responsibly to consider whether they should go for clearance? That would be through the introduction of some sort of sanction, perhaps a fine, on those who did not go for clearance and were found to have done something they shouldn't. At the moment, we go after them with our anti-avoidance powers and, as I have explained, we try to secure redress, but we have no sanction attached to that, so that is one angle. Then the other thing—

Q3466 **Chair:** But you would like a redress, wouldn't you, with sanctions?





**Lesley Titcomb:** We think it is worth exploring, but we need to understand two things: first of all, would it really have the desired effect; and secondly, can we attach it to the right people? Can the law attach the sanction to the right people? The second point it then raises is: can you use a clearance-type mechanism to improve member protection in some way? You could see here that you could bring it forward—at the moment our anti-avoidance powers act retrospectively. We look back after the event and take action, so you might bring the point of intervention forward then and say that in a certain—and I stress—limited number of circumstances schemes should come to us for clearance, because we can then ensure that the scheme is properly looked after in the transaction and can flag any concerns we have at that point.

There then comes a question: should we be given what we referred to as a hard block, the power to stop the transaction? We could only be given that if that number of schemes and situation was very tightly defined; if timeframes and so on were applied to us, so that we could not hold things up for ever and ever, and obviously it would have resource implications for us. It is something that is superficially attractive, but we absolutely have to be clear that we can achieve it without gumming up the entire works of British industry in terms of corporate transaction.

The other one big advantage it has is that, if you move to pre-clearance, you shift the costs on to the specific parties, whereas at the moment the costs of an anti-avoidance investigation fall on the people who pay the pension scheme levy because we cannot recover our costs.

Q3467 **Steve McCabe:** At the moment, its use has declined because people are not quite as anxious as they were initially—

**Lesley Titcomb:** That is our belief, but I think we need to detach that—

**Steve McCabe:** —and are a bit clearer about how anti-avoidance might be used, but the benefit of having some kind of compulsory element, if it was properly defined, is that it would shift the costs?

**Lesley Titcomb:** That is one element, yes.

Q3468 **Steve McCabe:** It would give you greater power where there was a real problem likely to emerge, and it might be healthier if it was coupled with the power—again, in tightly defined circumstances—to block the transaction. That is what you say you want.

**Lesley Titcomb:** We believe that is worth exploring, yes. We are at the early stages of that and we have to understand whether it can be defined in a workable way

Q3469 **Steve McCabe:** How do you propose to explore that? What is going to happen?

**Lesley Titcomb:** You are receiving the Minister for Pensions shortly, and you will be aware that the DWP is doing a range of work across DB schemes, which includes looking at some of our powers, and we are



## HOUSE OF COMMONS

discussing these ideas with them—many of the ideas that we set out in our letter to you, Chairman.

Q3470 **Steve McCabe:** One last thing. You mentioned the notice of deterrent fines as an extra power as a way of dealing with this. What level would a fine have to be set at to be a deterrent in your experience?

**Lesley Titcomb:** That is a very interesting question. Because we are dealing very often in these anti-avoidance cases with huge sums of money, the fine would have to be quite large in order to constitute a deterrent, I suspect. As I have said also, critically, it would have to attach to the right person to give the right incentive. I am aware that there is developing academic thinking out there on the deterrent value of fines and that kind of thing, which is why I think we would need to explore this further because it is an open debate as to whether fines do have that effect.

Q3471 **Chair:** If you had a range of fines, it would not be academic. We would actually know what worked, wouldn't we, after a while?

**Lesley Titcomb:** That is true. In other areas of our work we do have fining powers already. This is just one very specific—I suppose one might think of it more in this case as an incentive rather than a fine.

Q3472 **Chair:** Lesley, I cannot believe this Committee is going to advocate anything that stymies British industry, but if we look at the export of works of art, it is possible for the Government to hold a sale up for a very limited period of time to see if it can be sold and the money raised in this country. It would not be impossible for you to have similar powers, would it, about holding out for a limited period of time as settlement until you were satisfied?

**Lesley Titcomb:** That is exactly right. I believe that we should be careful about imposing costs and delay on people who are behaving properly, so we need to try to circumscribe this carefully if it is to be made to work.

**Chair:** Lesley and Andrew, thank you very much indeed for your evidence today. No doubt I will have more letters coming to and fro following today's hearing. Thank you very much indeed.



## Examination of witness

Witness: Richard Harrington MP.

Q3473 **Chair:** Richard, welcome to your first hearing before us. We have been looking forward to meeting you. Might you identify yourself for the sake of the record? Then Richard Graham will begin our questioning.

**Richard Harrington:** It is a pleasure to be here, Frank—may I call you Frank?

**Chair:** Yes, please do.

**Richard Harrington:** Or is the tradition Mr Field?

**Chair:** No, Frank.

**Richard Harrington:** When I was before the Home Affairs Select Committee it was much more formal. Frank, I am delighted to be here and I will obviously do my best to answer any questions you have.

**Chair:** Thank you.

Q3474 **Richard Graham:** Minister, welcome. We have been discussing with others, as you know, issues around DB pension schemes. The Green Paper that the Department is going to launch shortly will no doubt cover some of the areas we have been discussing. Would you like to give us a starting idea of what you hope might emerge from the process of Green Papers and White Papers and, ultimately, legislation? What sort of issues would you like to see resolved through legislation?

**Richard Harrington:** The first thing I would say is that what I found in pensions is that there are lots and lots of people who identify the problems—I think Steve Webb said this, and he was absolutely right—but solutions are a lot harder to find.

**Chair:** He did not have this Committee to help him then.

**Richard Harrington:** That is very true, and that is why I am very pleased to be here.

I want the Green Paper to be more than just another consultative document, because I think that the Government have to lead on issues. The issues, which you will all be very familiar with, as I can see, would be: consolidation, so the argument, which again is something that is endlessly said—the PLSA said it in their report—that there are far too many fragmented pension schemes. I can go into more detail if you like, but maybe we will be discussing it later. One heading would be consolidation. Can Government do anything? Can they not? On the Pensions Regulator, I saw Lesley Titcomb, the chief executive, just as I walked in. I don't know what you discussed with her, but does the regulator need more powers or is the system broadly correct? They are two things.



## HOUSE OF COMMONS

There are a lot of the governance issues around pensions trusts. Is the system of trusts, which has been the stalwart for so long, the correct one? It is all of the issues that you would know: the system of valuation, asset classes. I am afraid I cannot give you any magic ones because you know the headings, but it has to be a comprehensive look at all these points that are continually made by commentators in articles, by informed people, but Government do have to lead on them. Each one of them is extremely complex because it is all about—as I am sure you are aware, Richard—the rights of the individual, consumer protection, the rights of the Government—because Government are contributing by the tax relief system—and the rights of the sponsoring company themselves, because obviously the prosperity of the company is important, and not only to shareholders but to employees and obviously to the Government, because of all of the governmental issues. Everything is a balance and nothing has a simple solution, but I think the Government have to lead and I am not frightened of doing that.

What I don't want it to be is another kicking of the can down the road, because some issues are extremely difficult, but it is for Parliament—specifically for Government and DWP—to get to grips with them, so I am hoping it will be comprehensive but not just a general conversation. Many people have brought out reports that are a general conversation saying, "What's wrong?"

**Q3475 Richard Graham:** Thank you. I think the session today will hone in on some of those issues, Chairman. To be specific, in terms of the balance of responsibilities, clearly one of the most difficult balances is both making sure that the pension scheme is able to be supported by its sponsor and that, therefore, we are not impeding the sponsor's growth, while also contributing to things like PPF through the levy. What do you think Government might do to make life on the one hand a little bit easier for businesses? For example, what is your feeling about regulating to allow schemes to use CPI as the measure of indexation?

**Richard Harrington:** I will attempt to answer that question on indexation, but first I would like to state that we have to remember that to me a defined-benefit scheme is fundamentally not negotiable, inasmuch that it is an obligation of a company in the same way that salaries are, or leases on buildings. It is not an optional service charge as on a restaurant Bill; it is a commitment.

**Chair:** It is a property right, Richard.

**Richard Harrington:** Yes. That is a good way of putting it, Frank. It isn't that anything is negotiable. By the way, that does not mean that bits couldn't be negotiable. To use my analogy, or your property right analogy, many a time companies sign property leases for office buildings. They find they do not want it, the landlord could probably take possession of the building and bankrupt the company, but they don't. They negotiate it. That does not mean it is totally written in stone, but I think we should



## HOUSE OF COMMONS

remember that the core of it is that the pension is as much an obligation of that company as is any other liability.

As far as the system of indexation is concerned, I was quite surprised when I first looked at this to find what a difference it makes, because in my previous lives, politically and everything, I just thought it was the bit to do with mortgage interest and logically, before one thinks in detail, you think well, for pensioners mortgage interest is of less importance to their pockets than all of the other things that go into it.

Of course, when I looked at the numbers, I saw that the difference is very significant. When inflation is low it can be up to 50% more. I have the numbers here, but I am sure you will be very familiar with them. We are talking about in 2014 CPI was 1.5% and RPI 2.4%. It is very significant. When inflation was a lot higher it did not really make that much difference as a percentage.

So it is very significant and I have to think that we cannot just change things willy-nilly because it suits. I am sure in future it might be—I hope not—that inflation is higher. Things do change and the differences less so, but at the same time I think we have to remember that the reason these clauses were put in was to protect pensioners against increases in the cost of living. Even if they said specifically RPI or specifically CPI, I am sure the intention of the lawyers who drafted it was just to make sure that the pensioners were protected; it was not to go into some deep discussion about the difference in valuations—I think the Government were probably a lot more aware of the differences in calculation, but Governments switch from one to the other.

So in principle I have no objection to giving trustees, the people running the pension funds, the right to change the indexation, as long as there is the consumer protection so that pensioners are protected for what was intended, which was to be protected against rises in prices.

One thing does concern me, and it is a point of principle: the credibility of pensions in people's minds means that you force a change in the scheme rules, or even the Government gets involved, with very rare cases, because we do not want to undermine the whole principle that people can trust the pensions. We do not want people to think that they are just out to fiddle them again. I am open-minded, but it is precisely the kind of thing that the Green Paper needs to be going into in detail. If the principle of most things is that you get protected against prices going up in your field, which is how you would live as a pensioner specifically, I have no point in principle against changing the system of calculation.

**Q3476 James Cartlidge:** I was going to reflect on the first evidence session we had when the CBI was on the panel, and the impact that this measure has on the deficits ultimately. I was surprised at how significant the people that we had on the panel felt this was and to what extent changing this will impact on the number of firms that are potentially going to be looked at by the regulatory sector.



## HOUSE OF COMMONS

**Richard Harrington:** You are right to mention it. On paper the number is huge. I think it takes care of—this is newspaper headline stuff rather than detail—out of £400 billion deficit, or theoretical deficit, it would amount to £100 billion. It is a huge amount, but of course it is much more complex than that, because it is not like you snap your fingers and suddenly one quarter of the deficit is gone, or anything like that. In terms of newspaper-grabbing headlines, I would agree it is very significant, but it is just part of the picture.

It may well be that as time goes on the difference between the two headings of calculations change. It could be that the Government generally decide on a different form of calculation to reflect the change in people's lives. For example, just say that more people generationally become renters of property rather than people that have mortgages—I am not commenting on whether it is a good or a bad thing, or whether it will or will not happen, but things do change—or that food gets disproportionately more expensive. There are all sorts of things and then Government, for their own reasons, can decide quite properly, whatever shade of politics they are, to change the system.

We do not want pensions changing like that. What matters to pensioners is that their incomes are protected; it is a crude thing, but for their baskets of expenditure, whatever that might be at the time. I would totally agree with what you have said, James. To me on paper the numbers are huge. They are much bigger than at first thought.

Q3477 **James Cartlidge:** I said that it reminds me of the banks and their reserves. After the credit crunch banks have to hold much bigger reserves, but if you said that we have changed the measures and you do not have to have so much, that profoundly affects lending and the economy as well. In terms of this other balance that Richard mentioned, which to me is the most important point, about the impact on the wider economy, that would be very significant potentially in terms of investment.

**Richard Harrington:** I would just remind you that we cannot have people thinking they have been fiddled. That is important as well. We do not want people to say, "Oh, great. I'm making more money out of it going up because of the inflation calculation than affects me." But I am very aware of the fact that this is like the probity of the system of pension funds and we have difficulty enough in that when people read about BHS, Tata and all the things that I know this Committee has discussed at length. We cannot do too much fiddling about, but I feel comfortable as long as pensions are protected with what in real terms is the real difference to their income brought about by inflation, because that was the intention of doing it in the first place.

Q3478 **Steve McCabe:** I certainly agree with you about protecting pensioners. In that vein, the recent cases suggest that there are some pretty obvious lessons that can be learned about the regulatory framework as it affects defined-benefit pensions. What lessons do you think you have learned at



the moment and what changes are you inclined to make?

**Richard Harrington:** Well, Steve, I know that you are referring to exceptional cases, which is what you have said. I presume you are talking for example about BHS and Tata, but with this kind of headline-grabbing exceptional cases, and they are exceptional, it does seem to me that the purpose of regulation in any environment is to deal with the exceptional, not the normal. If you are talking about criminal stuff, we have a Theft Act; 98% or 99% of people would not dream of thieving, but we still have a Theft Act. So I do accept the fact that the purpose of regulation is not to deal with the norm, but to deal with the exceptional, without making it too prohibitive for the norm.

The regulator has to have the powers they need to deter and tackle misbehaviour and it could be that the regulator's powers are not enough. I was not present at the previous session, but I am sure that is what you were questioning Lesley Titcomb on. She has publicised in two press interviews that she might be looking for more powers, and that is her job.

**Chair:** She has moved considerably from our first meeting with her, Richard. She is now after more powers.

**Richard Harrington:** That may be, Frank, and I think that is exactly what the Green Paper should be looking at. The core issue is this: at the moment the pensions regulatory system was set up to be effectively after the fact. Most of the powers exist after the fact. In other forms of regulation that I have read about—in wealth management, for example, the FCA has a lot of more pre-emptive powers.

Q3479 **Steve McCabe:** Could you give us some idea? You said earlier that you do not want to kick the can down the road and we know there is a Green Paper at some point, but what in your judgment are the kinds of powers that might be needed? What is it that you think is not dealing with these exceptional situations?

**Richard Harrington:** I will come on to that, if I may. I am not trying to dodge the question. It is absolutely critical, but I am saying that at the moment most of it is reactive—and I keep calling the regulator a “she” which is incorrect; the chief executive of the regulator is a she—but it, the regulator, has those powers and we know about the notices that have been served and all this kind of thing. The sorts of things I think we should be looking at, for example, are more powers about information. What information is the regulator entitled to on a day-to-day basis to pre-empt the sort of thing that you are talking about, Steve, for example the exceptional points?

Should it be action after the fact, or should it be retrospective? That basically means: should the regulator have the power to intervene earlier? Should the clearance procedure, which is now voluntary, be made compulsory? Many other things in law are made compulsory—for example, corporate activities, monopolies and mergers before the



## HOUSE OF COMMONS

European competition clearance—so it is not unknown. To what level should the powers be more supervisory, as they are in the FCA?

Now, I did say that I did not want to kick the can down the road, but given that we are having a Green Paper on it, and it is soon, it is not one of these “one day, some day” things, I think the Department said in the winter. Well, I am hoping that it will be before the green shoots appear even in parts of Scotland, but this is a serious point and we need a vehicle to co-ordinate what people have been saying and, if necessary, bring legislation forward.

Many people argue that the regulator has powers that are not widely used. That is something that has to be looked into. It is something that she has been questioned on as the chief executive, and I know she is very aware of it. From my point of view, anything is on the table. Pensions regulation is comparatively new compared with other forms of regulation. As a Government Minister, a Conservative and a person who tries always to see both sides, my instinct is not to have over-regulation, but if there are cases where people are not deterred by current regulatory powers—most people behave properly, but some don’t—then we will have to change it. I cannot be more specific than that, Steve; not because I am hiding anything, but because I feel that is precisely what the Green Paper is for.

**Q3480 Steve McCabe:** The Committee can take away from this that you are thinking about possibly a supervisory role; you are thinking about an entitlement to access information, and compulsory rather than voluntary clearance if that is the obvious route to take?

**Richard Harrington:** You are pushing it a bit by saying that I am thinking of it; what I am saying is that it is exactly the sort of thing that we should be discussing. Yes, that is absolutely correct.

**Chair:** It will be. Great. James?

**Q3481 James Cartlidge:** There is a really important issue of moral hazard here. Are you confident that the moral hazard safeguards in place are adequate to discourage employers from dumping or neglecting their schemes?

**Richard Harrington:** Moral hazard is very difficult even to define. I know about moral hazard in terms of what the whole PPF and everything was set up for, but it is a very difficult thing to decide. What specifically in the context of this question do you think moral hazard is, before I can answer it?

**Q3482 James Cartlidge:** How fundamental do you want to get? With any system of state support there is a risk that people will not do their duty because they think they can be bailed out. That is the bottom line. There will be businesses out there who in theory might not act entirely in a good manner because they think the state will take over the tab.





**Richard Harrington:** I can think where someone has talked about putting it on the 3 o'clock at Haydock to make sure it is right and then if that does not work then the PPF will pick up the tab. So is that really what you mean?

**James Cartlidge:** Absolutely.

**Richard Harrington:** Yes, it is the PPF point. My instincts are that it is about right now, and there is no evidence of irresponsible behaviour just on the basis that the PPF can pick up the tab at the end of the day. I have not seen it, the PPF have not reported it to me and I have visited them and I meet very regularly with them. I do not quite know how to put this, but certainly no examples of that kind of irresponsibility have been brought to my attention and our tentacles are out everywhere to try to find out what is going on.

The fear is more on the basis of—as I am sure you are aware—changing the interest rates and bond yields and those issues, changing the parameters either because of a formal system of valuation or because of a fear of mixing up short-term commitments and theoretical deficits in the long term.

In terms of the whole original moral hazard issue, which was the fear of the Government just picking up the pot as people behaved irresponsibly, I have not seen any evidence of it. But it leads to all sorts of issues, doesn't it? For example, should independent trustees, or indeed trustees, have a specific governance responsibility? Again in other systems of regulation, often non-executive directors, if I could use them as comparable with trustees, have specific governance roles to the regulator. It might be about risk and so on, in non-pension worlds, but all this is to do with protection against. It is not just this moral hazard thing of being able to dump the PPF. It is if people go with the PPF—and I think it is a fantastic organisation and I congratulate those people who have set it up—but if you call it a haircut or a discount or whatever it is, it is not perfect for everyone and I think people know that, but I think we do have the balance about right on that.

Q3483 **James Cartlidge:** No, this would almost certainly be people coming in some way in distress, or about to enter a period where that might be the case, so I suppose this is really about getting information and therefore how proactive we should be.

**Richard Harrington:** Again, I think about what I flagged in answer to Steve McCabe's question about compulsorily providing information and more regularly, because it seems to me—and I know I did the politician thing and said it seems to me to be the sort of thing we should be thinking about, and it won't look very good in *Hansard* because it sounds like I do not know—that it is exactly what we should be looking at. I have not seen evidence of the kind of casino-type desperation behaviour from trustees where they are thinking, "Well, I might as well double my money because at the end of the day the PPF are looking after it." PPF is no cake



## HOUSE OF COMMONS

walk; it was never intended to be. They have their very long and comprehensive systems of due diligence. It is not just a case of saying that the Government have a bank account over at DWP that will pay it, so I think the balance is right.

**Q3484 Richard Graham:** Can I just come in a little bit on this business of getting information to the right people at the right time, which you said is the sort of thing you would want to look at? We took evidence from the guy who runs PPI, from Jeannie Drake from the Lords, who has been a trustee of many schemes, your predecessor, and UNISON, and they all agreed that the current situation where there is no obligation for either the sponsor or the scheme to provide information to the regulator if it requires it was totally unsatisfactory and needed to be provided for under law. Surely that is something that must play a part in the Green Paper, mustn't it? Alongside that, there is the business of the speed of valuations, which can take up to 18 months to provide. What is your feeling about resolving both these issues and what sort of role will they play in the Green Paper?

**Richard Harrington:** They will be very prominent in the Green Paper. Although I have said it is the sort of thing we should be thinking about, I would strengthen that in those two particular issues, because both of them are very critical. In terms of the timing issue, I cannot see why, looking at it from above and outside, it could not be done more quickly. It is professionals doing it. Very complex valuations get done in other fields. If somebody is selling a business, and I am sure they have instructed Savills or somebody to value 100 properties, you can be sure it would be done like that. I know it is more complex than that, but I cannot see why it should take a couple of years or whatever.

**Q3485 Richard Graham:** Well, BHS certainly sold the business in quite a hurry.

**Richard Harrington:** Exactly, and look what happened, but unfortunately your example is not a good one because of what happened. The fact is, where there is a will there is a way and, without prejudging the Green Paper, I cannot see why it should not be shorter.

In terms of information, I think businesses generally know—and there is no reason why pension funds are not the same—that part of doing business or part of operating a pension fund is that certain things that people might just write off as senseless bureaucracy is not senseless; it is providing a standard form of information. Remember that we are talking of tens of millions, or indeed hundreds of millions, of pounds so my instincts, without pre-empting the Green Paper—you ask me a straight question and I will try to give you a straight answer—are completely with what you said and with what Jeannie Drake said.

**Q3486 Luke Hall:** Minister, in your opening statement you mentioned consolidation and the amount of fragmented schemes. I wonder if you could perhaps just give us an update on your Department's work on consolidation and how that is progressing.



## HOUSE OF COMMONS

**Richard Harrington:** Again, it is one of the things; it is like the old “Hands up all those who are going to sin.” Nearly everyone would put their hand up. It is so obvious, it seems to me, that many pension schemes are subscale in a number of ways: subscale to getting good-quality management; subscale to invest in anything other than bog-standard types of investments; and subscale in terms of having specialist governance in the sorts of things that you need. It is easy to say that, and I am very proud for that to be on the record, but it is absolutely obvious.

It seems to me—you asked what my thoughts are—that there are different types of consolidation, and the Government have done it enough times to force it in non-pension things, like back-office consolidation where you share accounts departments and that sort of thing. In my opinion that sort of stuff does not work. I have seen it in local government in my own constituency, where it looks great on paper to merge two finance departments or two housing departments, but for the people working there, the management, they have two bosses. So they always have conflict because in this case there would be two sets of trustees, there could be two sets of councillors, or whatever the organisation is. It is one of the things that sounds good on paper and probably does not do any harm, because you do save overhead, but it is not really answering the question.

Then you move up to the second type, which would be—this is a bit like where the Government have nudged local government—where you have a block of money so they all put their money together, in the crudest terms, so you are saving money on management and being able to buy some sorts of different assets because you have specialist property people, hedge fund people, people looking at infrastructure and that sort of thing, but in the end you still have all these different groups that are reporting to individual ones, because companies still want the same control. The advantage of it is that there is a load of money there to invest more wisely in better things and save some costs, but then you also have the problem of dealing with all sorts of different top structures with all sorts of different interests, because it is an individual pension fund with different circumstances.

Again that is not a bad thing—I am not saying it is a ridiculous thing to do—but it does not really answer the problem, which is that we have far too many subscale, fragmented schemes where I imagine some sponsors, some companies, would be quite happy, providing their pensions were protected, not to be directly involved in the management of it through a trust. You could argue that then they could sell it to an insurance company, but we all know that costs a premium and they lose all forms of control. It could be that many companies would look at it if there was a non-PPF but a full-level type of PPF where they could put the money in, knowing that they could put in their contributions in the future and their members would be protected. It would be very difficult to do in practice, but that must be the nirvana.



## HOUSE OF COMMONS

If, for example, we are talking about increased regulation, as Richard and others have mentioned, the costs of regulation can in itself trigger consolidation because of the small schemes. It would be to do with information and reporting and things that to a big firm probably would not be very much at all, but if you are running a £5 million scheme it would be difficult to do.

Yes, I think the Government have to nudge consolidation. As a Government it would be impossible to start legislating and saying, "We are just going to take over all schemes with assets under so-and-so and make them into one big scheme." But I think it is so sensible and so obvious to do. We have to be able to find a way to do it that alleviates the fears of employers, many of whom are decent employers. They know their responsibility. They just know that for the moment they are going to put less money in but it is planned they are going to put more money in at other times. We have to find a way to alleviate their fears that suddenly they are going to lose control, obviously protect the members, and I do think the members were protected more with big scale than not, but protect the members.

I think it is not something to do like that, but we have to do something. We cannot just keep endlessly talking about consolidation without doing something. In the PLSA's initial report, which you may have read, again there is a whole bit on consolidation, but now they have been tasked with the detail of it, which is precisely the conversation we are having now, and I look forward to receiving that and I look forward in the Green Paper to receiving many people's ideas, but they have to be not just identifying the problem.

**Q3487 Richard Graham:** On consolidation, I am sure you are right to talk about scale, but of course sustainability is the other key issue. The Pension Protection Fund said to us, "We recognise there are a number of schemes and employers whose promises may now be unaffordable and a specific regime with suitable safeguards would be appropriate." What opportunities have you or your officials had to talk with the PPF about what they have in mind, and is that something different from what you are expecting the PLSA to come up with, or will the two be complementary?

**Richard Harrington:** I have not discussed that particular thing with the PPF. I have met them many times and we have a meeting and I will bring that up with them, so I cannot say that I have discussed it with them. It just seems to me—again, this is not Government policy—that there must be some kind of product or system that involves a non-PPF PPF that is at full level, not at a discounted level, where small subscale funds would be quite happy to put their members' money and benefits into, knowing that they are going to have a chance of getting better returns. For example, in my own constituency the biggest employer is Camelot, which is owned by the Ontario Teachers' Pension Fund.

**Q3488 Richard Graham:** Just in terms of the small and possibly unsustainable



## HOUSE OF COMMONS

schemes, the issue is going to be that for so long this has in theory been possible to do on a voluntary basis, but in practice nothing really happens unless there is legislation around it.

**Richard Harrington:** You are absolutely right. If I may, Richard, I will just come on to the small pot thing, which is a slightly different issue but not a ridiculous issue at all—it is absolutely a sensible one. But in terms of the non-PPF PPF that I was talking about, it just seems to me that if there was such a vehicle, a properly managed commercial vehicle, the advantages of those schemes, and I mentioned Camelot and others, where you need a lot of sophistication and obviously you cannot put a big percentage of your money in—nobody would be suggesting that—but to be able to invest in those things you need a big bulk to start with, so it remains a small percentage, infrastructure, all the other alternative investments, big commercial property, commercial residential.

There are lots of things and it is not for me to say what is a good scheme or not. I do not know what is or is not a good investment scheme, but it seems to me that if you only have a few million pounds, you cannot even consider them anyway. So there would be that ability to get those different alternative asset classes. There would be, I am sure, big management changes in the cost of management, simply because of specialisation and spreading the cost. I am sure it costs much the same in terms of calibre of fund manager if you just add zeroes to not. It is hopefully the same professional level of person that makes the decision and so on.

In terms of the small pot, which I think was your second question, basically if I am correct you are talking about the large number of small funds where no one is particularly interested, the zombie type of funds, where people have moved on to other jobs, they have their small—

**Richard Graham:** That is a separate issue.

**Richard Harrington:** Sorry, I misunderstood.

**Richard Graham:** That is really on DC schemes where you have individuals.

**Chair:** Yes, we are going to come on to that.

**Richard Harrington:** Sorry, I misunderstood.

**Richard Graham:** This is really about small DB schemes.

**Richard Harrington:** Yes, so subscale, operating DB schemes.

Q3489 **Richard Graham:** Where there may be in theory benefits both for the scale point and on their sustainability by merging together under one form of umbrella. In theory that has always been available on a voluntary basis, but in practice very little happens and therefore the question is whether legislation is really the only way to make this happen.



**Richard Harrington:** I fear that in that case it is. I think it is something that has to be seriously considered, but there are difficulties, as you know. How do you word legislation when some funds might quite legitimately not want to do it? So there is an element of which it has to be voluntary and why should the Government force you to do it? There are other examples in law.

Q3490 **Richard Graham:** It is an enabling mechanism?

**Richard Harrington:** Yes, and I was going to say where a system is set up because I think it would happen naturally, providing the mechanism was set up.

**Chair:** Right. Can we stay on that issue with Karen?

Q3491 **Ms Karen Buck:** Yes, it is the same thing. It is about what the scope is for allowing the small pots, for that to turn into lump sums and whether the rules should be relaxed to allow that to happen?

**Richard Harrington:** I think it is exactly what we should be looking at.

Q3492 **Ms Karen Buck:** What would be the process of doing that? Obviously that then starts segueing into a whole range of issues about lifetime allowances and tax treatment and so forth. Should the Government be incentivising it?

**Richard Harrington:** The overriding thing has to be consumer protection. It is fundamental. There are two real elements: consumer protection and the tax, because things trigger tax payments and suchlike. So this is something that we could not just look at from a pension point of view.

Q3493 **Ms Karen Buck:** But in many cases the funds are so small. The consumer protection angle is arguably less significant.

**Richard Harrington:** Not really, respectfully, because of course it already exists that people with £30,000 or more have to take professional advice, but for the small ones you are referring to, which I feel in the same way—well, I don't know if you think they are the most vulnerable, but I think they probably are. At the moment there is no compulsory system of advice for those people, yet if it is done properly it would be in their interests to do it. I know this sounds like prevarication, but it is not. We have to look at every single detail because, as you say, there are unintended consequences. Many a thing starts with the best intentions.

Q3494 **Ms Karen Buck:** There do; it is just that when we are into discussing sums so small, as many of them are, literally only a few thousand pounds, and I know it is a huge amount of money for some people, but then the cost of advice set against that starts becoming disproportionate. There is potentially an argument that says that by all means let us look at consumer protection when we are dealing with life-changing sums of money, but when we are starting to talk about a few thousand pounds only, maybe that really is just for individuals to make their own decisions.



**Richard Harrington:** Certainly. Government have done that before, with the £30,000 advice level and so on. I do not think any of us would want a free-for-all either, where the kind of people who hover around vulnerability—I am sure that members of this Committee will have seen the announcement over the weekend about cold calling. Although it is a Treasury announcement, it did come about because of people taking advantage of another form of freedom that people had. They varied from pure criminals, which is basically fraud by another name, to people who had schemes that were, we could sit here and say, “dodgy investment schemes,” and I am sure they would justify that they were not. I do not think we can just completely leave people from a consumer protection point of view. We cannot really say, “Well, it is a small amount; it does not matter” because, as you pointed out in your opening sentence, Karen, one person’s small amount of money is another person’s really significant sum.

Q3495 **Ms Karen Buck:** It is. We both agree on that. What I am arguing is that once you start imposing restrictions on relatively small amounts of money in cash terms, the cost of restrictions, mandatory advice and so forth starts to become disproportionate—

**Richard Harrington:** Yes, you mean if it is £500 minimum and the whole thing is £3,000, something like that? Yes, it is a difficult question and I am afraid it is one that I cannot give you the answer to. It needs a lot of thought.

Q3496 **Ms Karen Buck:** I wonder whether the argument that you are making about criminal behaviour, about preying on people, is in a sense a different issue from that of pensions management. It is about data protection; about being much tougher on how people can sell telephone numbers and e-mail addresses to others and so forth, rather than trying to impose those restrictions case by case on things like pensions.

**Richard Harrington:** Yes, you could be right. The real answer to all of this is law. We are absolutely right to ban cold calling, but if you are a real scammer you are not going to say, “Oh, there is a law against cold calling, and therefore I will not scam by cold calling.” I think the key to it is it educates people and informs them, and it is Government’s responsibility, as we have shown with Pension Wise, TPAS and all of this, and with debt management and other things, to pay for, which we have done at the guidance level, be it through levies or directly, it is still the same insofar as it is paid for not by the consumer, but in the end it is education. However small the amount of money is, there has to be someone that people can turn to and ask, at least for guidance if not for advice, simply because for them it may be the largest single sum of money that they have ever had, and most people might just say, “What are you asking me this for?”

Q3497 **Ms Karen Buck:** Absolutely, and we will leave it on this, but it is also arguable—the flip side of that—that if that is the largest sum of money that they have ever had, £3,000 or £5,000, then leaving it locked up in a



small pot is another way of limiting their choices.

**Richard Harrington:** I agree with you that they should have it, and it is a question of coming up with a system that does not restrict legitimate people from doing what they want to do, to pay for a holiday they have never had or whatever. It is perfectly legitimate to do that, but to make sure they are not vulnerable to the unfair pressures that we have shown people have had up to now and that the Government are trying to legislate against.

It is a form of criminality but, ironically with society with the police and everything, the sort of fraudulent criminality that we saw with these bank scams, for example, has nothing to do with pensions, but it is preying basically on the same people, and the police clearly have dealt with it. The main thing that is stopping it, from what was told locally to me, is loads of newspaper articles about it, so that people know. That is not what I am worried about.

It is just they contact so many people knowing that they have some money and they appeal to people, "You have £3,000. Well, you could get £5,000" and probably there is a hotel somewhere. It is not like it is a complete fraud. One person's good investment is another person's irresponsible one, so I am worried about that, and we have to find a way to do it, giving consumer protection without saying that we are just going to stop you and make you keep it in your bank because it is the only thing we will allow you to do. It requires a lot of thought.

Q3498 **Ms Karen Buck:** Moving on to a different issue, it is the question about independent trustees, and particularly in respect of the management and governance of the smaller schemes where I think there is an issue about whether there is a sufficient number of people who could fulfil that function and whether again in terms of consolidation schemes, given the not unlimited pool of people who are able to fulfil that function and contribute to good governance—that is another argument. How can we strengthen the role of independent trustees?

**Richard Harrington:** First of all, I would like to say that I am very much in favour generally of professional trustees. I think it is a professional job. It is dealing with people's money and at the end of the day it is like school governors. It is a good thing to have school governors. We have all seen them work very well, but at the end of the day school governors' main function is to make sure that the management manage properly.

I think with pension trustees they need professional help by and large that is not the people managing the money. Obviously they are professional, or I hope they are; they are regulated; they are professional people. I think we have to accept the fact that in the new world it is much more complicated than it was, and we cannot just rely on well-meaning people or appointees of the employer. That is not in any way to say that there is a whole class of people who are not fit to be trustees, but it has





## HOUSE OF COMMONS

become much more complicated, and if there is more regulation, as had been called for, it will become even more complicated.

I think that there is much more a role for a professional and, if not professional in that they do that for a living, just professional, more independent, trustees. I certainly believe that governance responsibilities should be the role of trustees, specifically independent trustees, and we have to accept the fact that we have to look now at the role of trustees generally. Things have moved on. Things are more sophisticated. We have to have people who have the time to do it and are trained to have the responsibility to do it. So it is moving in that direction. I do think it is something that we should push, and again it all leads to consolidation because people need paying for their time.

Q3499 **Chair:** Very good. Can I just end, Minister, by thanking you for your contributions today, and on your Green Paper timing? Because Mhairi I do not think was here when you talked about spring in northern Britain.

**Richard Harrington:** Yes, I withdraw the comments about green shoots in Scotland; they are a little bit after England.

**Chair:** No, but there is a real difference when winter ends in this country. Can we tie you down a bit more about when you expect the Green Paper to be out?

**Richard Harrington:** Soon, Mr Field. Honestly, all efforts are on it. We have to get it right. It is not like months and months away. I cannot be more specific because I am pushing for it. I have one chance. We cannot blow this. We have to get it comprehensive and my instinct would be to have it out tomorrow, but like everything else in Government it is more complex. I would not like you or any member of the Committee to think that this is just a delaying tactic; quite the opposite. I want to get it right.

Q3500 **Steve McCabe:** If it is not out by April what will have gone wrong?

**Richard Harrington:** I hope it will be before then. Put it this way: I am taking a hands-on thing with this. I am meeting with officials. We have hour-long sessions on every single topic that could go in it. It is not just, say, some official writing paper and me ticking it off on a Sunday night when I want to watch telly.

Q3501 **Chair:** Richard, when you said you did not want your Green Paper to kick the can down the street, will it be different in the sense that you will present the problem that you said people are very good at presenting to you? Will you then present a number of alternatives on which you would like people to comment?

**Richard Harrington:** I would like to, and I think in certain of the cases the Government have to push towards, knowing that it is not a White Paper, of course; it is a Green Paper. There are a lot of very urgent issues here. I would like to just reiterate that this is not complacency, but everything is not on fire. We have to do this properly because the last



## HOUSE OF COMMONS

thing Government want, or I am sure any Member of Parliament or anybody wants, is for unintended consequences all over the place that no one has thought about.

**Chair:** Sure. That is really helpful, Richard. Thank you very much.

***Richard Harrington:*** It was a great pleasure coming in.

**Chair:** It was a useful session, and thank you for coming in by yourself as well.

***Richard Harrington:*** It was very nice of you to invite me. Thank you.